Insurance Bonanza for Intermediaries
written by Raghav Gaind | May 29, 2020

Increased FDI in Insurance Sector Strategy to Tackle COVID

The insurance sector plays a pivotal role in promoting the economy of every country. The market strategy used in the Indian markets for both life and non-life insurance is almost at the minimum level in comparison to the rest of the world. Enhancing the insurance business may lead to an increase in the economies of scale. The loosening of foreign investment returns in the insurance sector has been a hot topic of discussion, as it pertains to the interest of many stakeholders and participants of the industry. It is these very participants who encourage a surge in the percentage of Foreign Direct Investment (“FDI”).

The Reserve Bank of India (“RBI”) vide notification dated 31.03.2016[1] had increased the FDI investment in the insurance sector to 49% from an existing 26% based upon the terms and conditions issued through the notification dated 30.02.2016[2]. The main condition under this notification was under no circumstances ‘*any foreign investor shall hold more than 49% of the shareholding in any form*’. This means that the insurance company shall be solely in control of an Indian citizen or Indian resident or Indian corporate, as the case may be.

New Insurance Policy

Although the Indian government has allowed increasing the FDI to 49%, foreign investors were still not satisfied with the process bearings in running the business. Since the majority holding of the company lies in the hands of the Indian residents, foreign investors are automatically not involved in the key managerial decisions of the organisation. This resulted in a decline in the flow of funds by foreign partners. Nirmala Sitharaman the then Foreign Minister of India in her budget speech on 5th July 2019 had announced that the FDI limit for the insurance intermediaries will be increased from 49% to 100%.

In pursuance of this, on September 2nd,2019 the central government issued a notification[3] under the Indian Insurance Companies (Foreign Investment) Amendment Rules, 2019 (Rules) that the FDI limit for insurance intermediaries has increased to 100%. Now, the Department of Promotion of Industry and International Trade (“DPIIT”) through its press note vide dated 21.02.2020[4] increased the FDI in insurance intermediaries to 100%.

For the purpose of clarification, the FDI in insurance companies shall remain at a mere 49% but only in cases of insurance intermediaries which includes insurance brokers, re-insurance breakers, insurance consultants, corporate agents, third party administrator surveyors and such other entities as may be notified by Insurance Regulatory and Development Authority (“IRDAI”).

According to the Rules, there will be no cap imposed on the foreign equity investment for the insurance intermediaries. However, there are certain conditions that are imposed on the entities whose primary business is not insurance.

Rule 9 of the Rules provides that the implementation of the proposals of FDI in the sector of insurance intermediaries will be done through an automatic route with prior permission and the verification of the IRDAI. If in circumstances where the majority shareholders of the company are foreign investors, insurance intermediaries have certain conditions to fulfil:

- It must be registered as a limited liability entity under the Companies Act, 2013.
- It must be ensured that at least the chair of the board of directors or the Chief Executive Officer of the Company (CEO) should be a resident of India and must possess Indian nationality.
- The permission of IRDAI needs to be obtained for the repatriation of the dividend of the company and any dividend which is above 75% cannot be repatriated by an insurance intermediary.
- The entity must be incorporated with advanced technological and managerial skills for better and smooth functioning.
- There should be no payments that are not necessarily made to the foreign companies, promoters or subsidiary companies and associated companies that are not priorly permitted by IRDAI.
- All of the payments made to the foreign companies, promoters or subsidiary companies and associated companies must be in a properly specified format according to the rules of IRDAI.
- The board of directors and all the officials who are involved in the key management of the entity should be directed to properly follow the rules laid down by the associated regulators.

SKEPTICAL NATURE ON THE APPLICABILITY OF THE GUIDELINES ON INDIAN OWNED AND CONTROLLED (IOC)

The IRDAI notifies certain other norms apart from the Foreign Investment Rules which must be followed by the insurance companies and the intermediaries of the insurance sector. These entities must comply with all the aspects given under the "Guidelines on Indian Owned and Controlled" dated October 19, 2015[5]. According to these stipulated guidelines, all insurance intermediaries must be Indian owned and must be regulated by Indian laws at all times. To ensure that the functioning of the companies is controlled by India, the following requirements must be satisfied:

- The nomination of the Indian directors and the majority number of board members should be done by the Indian promoters and the stakeholders but this excludes the nomination of independent directors.
- All the officers who are in charge of the key management of the entity like the CEO and the chair of the Board of Directors including the principal officer must be appointed by the Indian promoters and the board of directors of the company.
- The board of directors who are appropriately nominated must have the authority to control and regulate the significant policies of the company.
- In the circumstances where the chair of the board of directors has the power of casting a vote, they must be essentially nominated by the Indian investors and promoters.
- When a board meeting is conducted the majority of the board members must be

Indians.

In response to the notification of the Rules, IRDAI did not declare a firm stance with regard to the continued applicability of the IOC guidelines to the insurance companies and its intermediaries after the limit of FDI on intermediaries had been removed. Therefore, it was considered that the IOC was overridden due to the introduction of the Rules.

CONCLUSION

Even though the introduction of 100% FDI was hugely welcomed by the intermediaries in the insurance sector, the domestic players were not that convinced with this initiative. There has been a mixed reaction in the market. It will have a positive impact on the major players of the insurance industry. Although it will increase the foreign investment in India, there will be a huge amount of repatriation of money as the foreign investors will be looking for returns.

This policy of foreign equity which was initiated by the government may pose to be a severe threat to the Indian entrepreneurs who wholly own and control the domestic insurance intermediaries. It is yet to be ascertained with regard to the steps that IRDAI will take to prevent this adverse effect on the domestic players. However, such liberalisation will surely help India to improve its index on ease of doing business for the rest of the world. With this amendment, it is anticipated that the IPO of Life Insurance Corporation of India is a sure shot success.

- [1] https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10316&Mode=0
- [2] https://www.irdai.gov.in/ADMINCMS/cms/frmGeneral_Layout.aspx?page=PageNo3946
- [3] https://dipp.gov.in/sites/default/files/pn1_2020.pdf
- [4] https://www.irdai.gov.in/ADMINCMS/cms/whatsNew_Layout.aspx?page=PageNo2644&flag=1

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